Major Business Taxes in Kentucky

State Corporation Income Tax (KRS 141.010 et seq.)
Kentucky corporations and foreign corporations owning or leasing property or having one or more paid employee(s) in Kentucky pay an income tax annually on taxable net income. Exempted are banks and trust companies other than bankers' banks, savings and loan associations, production credit associations, insurance companies, corporations exempted from federal income tax under section 501 of the U.S. Internal Revenue Code, small business S Corporations, and other nonprofit religious, educational, and charitable corporations. (KRS 141.040)

Kentucky has adopted the United States Internal Revenue Code definition of corporation [(Section 7701(a)(3)], which includes associations, joint-stock companies, and insurance companies. However, some of these entities are then exempted from the state corporation income tax as noted above. The definition applies only to the income tax. [(KRS 141.010(24)]

- Limited liability companies that are treated as corporations for federal income tax purposes also are treated as corporations for Kentucky income tax purposes. (KRS 141.208)

Tax Rate Schedule

Taxable Net Income	Tax Rate (Per Taxable Income Level)
$0 – $25,000	4.0%
$25,001– $50,000	5.0%
$50,001 – $100,000	6.0%
$100,001 – $250,000	7.0%
$250,000 (plus)	8.25%

Source: KRS 141.040

Corporations having business income taxable both in Kentucky and elsewhere pay Kentucky income tax on that portion of business income earned in Kentucky as determined by the state's apportionment formula. The formula is based upon the Uniform Division of Income for Tax Purpose Act (UDITPA), which has been adopted generally by the majority of states. The Kentucky formula differs from the UDITPA formula in three (3) ways:

1. There is no throwback —sales are not recaptured to Kentucky when the sales are made to a state where the corporation has no tax liability;

2. Pollution control equipment owned or leased in Kentucky is excluded from the property factor; and

3. The sales factor is given fifty (50) percent of the total weight in Kentucky's formula. (KRS 141.120)

Kentucky's Apportionment Formula

Property Factor + Payroll Factor + Sales Factor (x2)
4

Note: Computed to four (4) decimal places.

Property Factor Equals (=)

Average value of real and tangible personal property owned or rented and used in Kentucky during the tax period	Divided (÷) By	Average value of all the taxpayer's real and tangible personal property owned or rented and used during the tax period

Note: Excluding certified pollution control equipment

The average value of property, as used in the property factor of the apportionment formula, is determined by averaging the values at the beginning and ending of the tax period. The Kentucky Department of Revenue may require the averaging of monthly values during the tax period, if it is reasonably required to reflect the average value of the taxpayer's property. Construction in progress is excluded from the property factor computation.

Property owned by the taxpayer is valued at its original cost, and property rented by the corporation is valued at eight (8) times the net annual rental rate (excluding receipts for sub-rentals).

Payroll Factor Equals (=)

Total amount of compensation paid or payable in Kentucky during the tax period	Divided (÷) By	Total amount of compensation paid or payable everywhere during the tax period

Sales Factor Equals (=)

Total sales in Kentucky (destination basis) during the tax period	Divided (÷) By	Total sales of the taxpayer everywhere during the tax period

Gross receipts are substituted for sales when figuring the apportionment of income for corporations providing services, rentals, or the licensing of tangible or intangible personal property. Special apportionment provisions apply to public service companies and financial organizations.

Sales to the U.S. government from a place of storage in Kentucky are considered as sales in Kentucky for state income tax purposes.

Multistate corporations can petition the Kentucky Department of Revenue for alternate apportionment formulas, when the statutory three (3) factor formula does not fairly represent the extent of the business activities in Kentucky. State statutes and regulations provide for special apportionment measures for interstate telecommunications companies, common carrier transportation companies, pipeline companies, regulated investment companies, securities brokerage companies, and loan companies.

Affiliated corporations may choose separate reporting or elect consolidated filing under Federal IRS guidelines. Election to file consolidated returns is binding for eight (8) years. Unitary combined filings are not allowed. (KRS 141.200) Corporations with an annual state income tax liability estimated to reach $5,000 or more must file a declaration of estimated tax and make installment payments.

Gross Income

Gross income of corporations subject to Kentucky income tax is similar to income reported for federal income tax purposes.

Excluded from Kentucky gross income is income exempt from taxation by the Kentucky Constitution and the Constitution and statutory laws of the U.S.; all dividend income; income from safe harbor leases; any amount received by a tobacco producer or quota owner from the master settlement agreement, secondary settlement fund, or commodity credit corporation; and fifty (50) percent of the gross income from any disposal of coal covered by Section 631(c) of the Internal Revenue Code, if no deduction is taken for percentage depletion.

Included in Kentucky gross income is interest income from obligations of other states and their political subdivisions (bonds, notes, mortgages, etc.,) and income from intercorporate transactions adjusted to an arm's length basis, when required by the Kentucky Revenue Cabinet to prevent the avoidance of taxes.

Net Income

Net income for corporations subject to Kentucky income taxes is gross income minus essentially the same deductions from gross income as allowed for federal income taxes, except for the following which are not deductible when computing Kentucky net income:

(a) income taxes paid to other states, U.S. territories or possessions, or any foreign country or its political subdivisions;

(b) any deduction allocated to income which is exempt from taxation;

(c) certain dividends received by the corporation (as defined by Sections 243, 244, 245, and 247 of the U.S. Internal Revenue Code); and

(d) amounts paid to any club, organization, or establishment that has been found by the courts or a government body to discriminate in its membership, privileges, or services on the basis of race, color, religion, national origin, or sex.

Depreciable property placed in service after December 31, 1989, is depreciated in the same way as allowed by federal depreciation rules in effect prior to September 11, 2001. Property placed in service during the 1980s is adjusted to the value used for federal income taxes, beginning in 1994. Kentucky has not adopted the thirty percent (30%) federal bonus depreciation enacted by the Job Creation and Worker Assistance Act of 2002, or the fifty (50%) bonus depreciation enacted by the Jobs and Growth Tax Relief Reconciliation Act of 2003.

Income Tax Credits
(For Additional Information see Kentucky Business Incentives fact sheet.)

a. Credits for up to one hundred (100) percent of approved costs, for up to ten (10) years, on land, buildings, site development, and building fixtures and equipment used in new or expanded manufacturing operations are available under the Kentucky Industrial Development Act (KIDA). Companies must create at least fifteen (15) new full-time jobs and invest at least $100,000. (KRS 154.28-090 and 141.400)

b. Credits for up to one hundred (100) percent of approved costs, for up to fifteen (15) years, on land, buildings, site development, and machinery used in new or expanded manufacturing operations in approved counties with high unemployment rates are available under the Kentucky Rural Economic Development Act (KREDA). Companies must create at least fifteen (15) new full-time jobs and invest at least $100,000. (KRS 154.22-050; 154.22-070; and 141.347)

c. Credits for up to fifty (50) percent of start-up costs and fifty (50) percent of annual rental costs or rental value, over a ten (10) year period, for new or expanding service and technology intensive projects that provide more than seventy-five (75) percent of their services to out-of-state customers and create at least fifteen (15) jobs for Kentucky residents are available under the Kentucky Jobs Development Act (KJDA). (KRS 154.24-110 and 141.407)
d. Credits for up to seventy-five (75) percent of the costs of upgrading manufacturing plants and equipment to prevent the closing of outdated facilities are available under the Kentucky Industrial Revitalization Act (KIRA). The credit can also be extended to corporation license taxes. (KRS 154.26-090; 154.26-100; 141.403; and 136.0704)

e. Credits for up to fifty (50) percent of the costs of equipment used to recycle or compost business or consumer waste materials and machinery used to manufacture products from recycled waste materials. (KRS 141.390)

f. A credit of $100 of each unemployed person hired for at least 180 consecutive days. (KRS 141.065)

g. Any taxpayer that is an electric power company or an entity operating a coal-fired electric generating plant may receive a $2 per ton tax credit for each ton of Kentucky coal burned. Coal purchases in excess of the base year 1999 calendar year are eligible for the credit. (KRS 141.0405)

h. A credit for up to 4.5 percent of the value of Kentucky coal (excluding transportation costs) used for industrial heating or processing, for ten (10) years following either the installation or conversion to coal burning units. (KRS 141.041)

i. A credit of up to $1,500 for ten (10) percent of the wages paid to certain unemployed or low-income individuals that are hired by qualifying enterprise zone businesses. (KRS 154.45-090)

j. A credit is allowed to investors in certified venture capital funds equal to forty (40) percent of their proportional ownership share of all qualified investments made by the fund, not to exceed fifty (50) percent of their credit in any one (1) year. (KRS 154.20-250 to 154.20-284; and KRS 141.068)

k. A skills training investment tax credit may be awarded by Bluegrass State Skills Corporation as a nonrefundable credit for a company's occupational or skills upgrade training program. The credit is equal to fifty (50) percent of the approved cost incurred and may not exceed $500 per employee and $100,000 per company. (KRS 154.12-2084 to 154.12-2089; and KRS 141.405)

l. The Kentucky Economic Opportunity Zone Act (KEOZ) focuses on development of areas with high unemployment and poverty levels. Eligible companies include new or expanded manufacturing, services, or technology industries, which must invest at least $100,000 in the project and create at least ten (10) new full-time jobs for residents of the zone. An approved company may receive up to one hundred (100) percent credit against Kentucky income tax liability on taxable income generated by the project(s). The credit over the term of the agreement shall be limited to the total approved incentive amount. The approved company may carry forward credits during the agreement term, which shall be for ten (10) years. (KRS 154.23-005 – 154.23-079 and KRS 141.401)

m. An employer is entitled to an income tax credit for a portion of released time given to assist an employee in obtaining a high school equivalency diploma. The credit is calculated by multiplying fifty (50) percent of the hours released by the student's hourly salary. The credit shall not exceed $1,250. (KRS 151B.127)

n. A state income tax credit equal to 5 percent of the qualified cost is available to new and existing businesses that construct, remodel, expand, or equip research facilities, but does not include replacement property. Any unused credit may be carried forward for ten (10) years. (KRS 141.395)

Tax Losses
A corporation in Kentucky can carry its Kentucky net operating losses back for two (2) years and forward for up to twenty (20) years for tax years beginning after August 6, 1997. A multi-state corporation sustaining a tax loss only at its Kentucky facility during its first year of operation can carry the loss forward as a deduction from second year Kentucky taxable income, provided separate accounting can be used for the Kentucky activity. (KRS 141.011; 141.012) Kentucky has not adopted the federal five-year net operating loss carryback rule enacted by the Job Creation and Worker Assistance Act of 2002.

State Income Taxes: S Corporations (KRS 141.040)
Kentucky income tax laws recognize small business "S Corporations" for special income tax treatment. Qualifying S Corporations can have up to seventy-five (75) shareholders (individuals, estates, or trusts) and must have a single class of stock.

- Kentucky has adopted the U.S. Internal Revenue Code definition of S Corporations [(Section 1361(a)]. [(KRS 141.010(25)]

The income of S Corporations is exempt from state income taxes, except when the S Corporation realizes certain levels of capital gains. S Corporations must pay Kentucky income taxes whenever their net capital gains exceed $25,000, and exceed fifty percent (50%) of its taxable income for the taxable year and its taxable income for such year exceeds $25,000. The tax is the lesser of (a) the tax determined by applying the corporation income tax rates to the capital gains in excess of $25,000; or (b) the tax determined by applying the corporation income tax rates to the taxable income in excess of $25,000. In no case shall the S Corporation pay corporation income tax if Section 1374 of the Internal Revenue Code would exempt such capital gains from federal income tax.

Stockholders of an S Corporation in Kentucky pay state individual income taxes on their pro rata shares of the corporation's net income accruing to them individually, whether or not the income is withdrawn from the corporation. Tax rates for an individual are as follows:

Tax Rate Schedule

Taxable Income	Tax Rate (Per Taxable Income Level)
$0 – $3,000	2.0%
$3,001 – $4,000	3.0%
$4,001 – $5,000	4.0%
$5,001 – $8,000	5.0%
$8,000 (Plus)	6.0%

Source: (KRS141.020)

The income of an S Corporation subject to taxation as distributive shares receives the same adjustments that are required by Section 1363 (b) of the U.S. Internal Revenue Code.

Nonresident individuals that are shareholders of an S Corporation, which does business both in Kentucky and outside of the state, are taxed in Kentucky on the income of the corporation attributable to business conducted in the state. This is determined on the basis of the proportion of gross receipts from sales or services provided in Kentucky to sales or services provided everywhere. (KRS 141.206)

State Income Tax: Proprietorships and Partnerships

Sole proprietorships and partnerships are exempt from state corporate income taxes. Instead, the owners pay state individual income taxes on their shares of the earnings of the businesses, regardless of whether they take the income for their personal use or leave it in the business. Corporate partners who are partners in a partnership doing business in Kentucky are taxable on their distributive share of the partnership’s income. If the corporate partner’s only business activity in Kentucky is the partnership interest, then the corporate partner is subject to Kentucky’s corporation income tax on its distributive share income multiplied by the ratio of the partnership’s Kentucky gross receipts divided by the partnership’s total gross receipts. Limited liability companies that are treated as partnerships for federal income tax purposes also are treated as partnerships for Kentucky income tax purposes. Although partnerships have no state income tax liability, they must file an information return annually. Income distributed from a qualified investment partnership to a nonresident partner is not subject to Kentucky tax. “Qualified investment partnership” is defined to mean a partnership formed to hold only investments that produce income that would not be taxable to the nonresident individual if held or owned individually. (KRS 141.206).

- A limited liability company, in Kentucky, is defined as any company subject to the provisions of KRS Chapter 275. Tax rates for an individual are as follows:

Tax Rate Schedule

Net Taxable Income	Tax Rate (Per Taxable Income Level)
\$0 – \$3,000	2.0%
\$3,001 – \$4,000	3.0%
\$4,001 – \$5,000	4.0%
\$5,001 – \$8,000	5.0%
\$8,000 (Plus)	6.0%

Source: (KRS141.020)

The income of partnerships subject to taxation as distributive shares receives the same adjustments that are required by Section 703 (a) of the U.S. Internal Revenue Code.

Owners of unincorporated businesses who earn over $5,000 each year without withholding for state income taxes and who have a state tax liability of more than $500 must file estimates of income and make payments quarterly.

Nonresident individuals that are partners of a partnership, which does business both in Kentucky and outside of the state, are taxed in Kentucky on the income of the partnership attributable to business conducted in the state. This is determined on the basis of the proportion of gross receipts from sales or services provided in Kentucky to sales or services provided everywhere. (KRS 141.206)

State Corporation License Tax (Franchise Tax) (KRS 136.070–136.100)
Domestic corporations in Kentucky and foreign corporations owning or leasing property in Kentucky or employing one (1) or more individuals receiving compensation in the state must pay an annual state license (franchise) tax. Exempted are banks and trust companies, savings and loan associations, production credit associations, insurance companies, public service companies, corporations exempted by Section 501 of the U.S. Internal Revenue Code, and nonprofit corporations. Small business S Corporations are subject to the tax. (KRS 136.070)

For license tax purposes, Kentucky has not defined the term corporation. However, limited liability companies, partnerships, and other non-incorporated entities are exempt from the tax.

The tax rate is $2.10 per $1,000 (0.21 percent) of total capital employed in Kentucky, with a minimum tax of $30 annually.

- Corporations with gross income of $500,000 or less pay the license tax (after a tax credit) at a rate of $0.70 per $1,000 on the first $350,000 of Kentucky capital employed and $2.10 per $1,000 on capital in excess of $350,000.

Capital employed is defined by state statutes as "capital stock, surplus, advances by affiliated companies, intercompany accounts, borrowed monies, or any other accounts representing capital used and employed in the business." Excluded are amounts borrowed to purchase inventories. Capital is reported for tax purposes at book value on the last day of the corporation’s tax year.

For those corporations having payroll or property both within Kentucky and outside the state, total capital is apportioned to Kentucky according to a three (3) factor apportionment formula. The Revenue Cabinet allows taxpayers to use the same formula as used for the corporation income tax. Double weight is given to the sales factor.

Kentucky's Apportionment Formula

$$\frac{\text{Property Factor} + \text{Payroll Factor} + \text{Sales Factor (x2)}}{4}$$

Note: Computed to four (4) decimal places.

If the three (3) factor formula does not fairly measure the taxpayer's capital employed in Kentucky, the taxpayer may petition the Revenue Cabinet for a variance in the application of the formula, or the Cabinet may require an alternate calculation.

Kentucky does not combine or consolidate multi-state or multi-national corporations for license tax purposes. Returns must be filed on a separate company basis.

Open end registered investment companies organized under the laws of Kentucky pay a state tax of $2.10 per $1,000 of "average net capital." Net capital includes capital stock, surplus, borrowed money, or other capital accounts, minus company-owned Kentucky state or local government securities. Average net capital is computed from net capital shown on the company's books on the first and last days of its tax year. (KRS 136.072)

- Corporation license tax credits for up to seventy-five (75) percent of the costs of upgrading manufacturing plants and equipment to prevent the closing of outdated facilities are available under the Kentucky Industrial Revitalization Act (KIRA). (KRS 154.26-090; 154.26-100; and 136.0704)

- A license tax credit of up to ten percent (10 percent) of the eligible costs is available to existing companies classified under NAICS codes 336211 (motor vehicle body manufacturing), 336111 (automobile manufacturing), 336112 (light truck and utility vehicle manufacturing), and 336120 (heavy duty truck manufacturing) for reinvesting in those industries. A project must have eligible costs of not less than $100 million to qualify for the credit. The credit may be taken for a period of up to ten years. A project eligible for this credit may receive final approval after July 1, 2004. This credit also applies to income tax. (KRS 154.34-010 – 154.34-100, KRS 141.415 and 141.416)

State Corporation Organization Tax

Corporations that incorporate in Kentucky pay an organization tax to the Kentucky Secretary of State. The tax is based upon the number of shares of capital stock authorized in the articles of incorporation. The tax is also levied on extra shares of stock authorized by amended articles of incorporation and on additional shares created by merger or consolidation. (KRS 136.060)

Shares of Stock	Tax Per Share
1 to 20,000	$ 0.01
20,001 to 200,000	$0.005
Over 200,000	$0.002
Minimum Tax	$10.00

Local Occupational License Taxes On Net Profits
Kentucky statutes allow cities, counties, and school districts to levy occupational license taxes on the net profits of businesses including corporations, proprietorships, partnerships, and self-employed individuals. The taxes may be levied either on a flat rate schedule (based on type of business or employment size) or as a percentage of local net profits or gross receipts. For businesses with payroll and sales in more than one tax jurisdiction, net profits or gross receipts are apportioned using an equal weight of a payroll factor and a sales factor. For businesses with just sales in more than one tax jurisdiction, net profits or gross receipts are apportioned using a sales factor only. A few cities and counties place a cap on the tax payable annually by an individual business or exempt the lower amounts of profits. Some exempt income from sales to points outside of the local area. (KRS 68.180; 68.197; 91.200; 92.280; 92.281; 160.482 through 160.488; and 160.605)

Exemptions

- Counties having a population of 30,000 or more are prohibited from collecting license fees or occupational taxes on profits, earnings, or distributions of an investment fund qualified under KRS 154.20-250 to 154.20-284 to the extent income would not be taxable to an individual investor. (New Section KRS 68.197)

- Cities of all classes are prohibited from collecting license fees or occupational taxes on qualified investment partnerships. (New Section KRS 68.197)

For current occupational license tax rates check the community information section.

Businesses file returns and pay the tax on net profits (usually once annually) to the city or county, or to both. When the tax is levied on payrolls, the business withholds taxes from the salaries and wages of its employees and submits them (usually once quarterly) to the city or county, as applicable.

State and Local Property Taxes (KRS 132.010 et seq.)
Kentucky's state and local property tax system differs from those of most states. State government taxes all property not specifically exempted by the state constitution or personal property exempted by the legislature. Local governments are prohibited from taxing certain classes of property, such as manufacturing machinery. Local taxing jurisdictions in Kentucky include counties, cities, school districts, and special taxing districts (fire protection districts, sanitation districts, watershed districts, etc.)

State statutes place a limitation on the growth of property tax revenues. Local property taxes may not produce more than a four (4) percent increase over the previous year's revenues from real property, excluding new property, without voter approval. Likewise, the state property tax rate on real estate is adjusted each year to limit the statewide revenue from this class of property to no more than four (4) percent above the amount for the previous year, including revenue from new real property, but excluding tax increment financing development areas and KRS Chapter 103 IRBs for industrial buildings from the state property tax rate setting rollback provisions. The provisions apply to aggregate real property assessments in a jurisdiction but do not limit increases to individual properties. (KRS 132.010)

Assessments (KRS 132.220; 132.280)
The basis of assessments for property taxes in Kentucky is one hundred (100) percent of fair cash value. The Kentucky Department of Revenue performs the assessment valuation for a limited number of classes of property including property owned by utility companies; railroads; airlines; most financial institutions; distilled spirits; nonresident commercial watercraft; and unmined minerals. The county Property Valuation Administrator (PVA), an elected state official, assesses all other classes of taxable property for the state, the county, school districts, and for most special taxing districts. Two cities in Kentucky make their own assessments, and all other cities use the assessments made by the county PVA. Assessments are based upon property held on January 1st of each year. Taxpayers are required to report the value of all of their taxable property to the local PVA annually.

For assessment purposes, guidelines concerning the definitions of various tangible personal property are important. A manufacturer is defined as an entity that purchases, receives, or holds personal property for the purpose of adding to its value by manufacturing, refining, rectifying or mixing different materials with a view of making a profit. While there is not a single statutory definition of manufacturing machinery, the courts have defined manufacturing machinery as that which gives new shape, new quality, or new combination to matter, and which changes the adaptability of the matter and converts it into articles suitable for use. Manufacturers' goods in process include inventory that was originally a raw material that has been acted upon in some manner but has not completed the manufacturing process. Manufacturers' finished goods represent products that have been manufactured and are ready for sale or shipment. The value of both goods in process and finished goods must include all factory burden and overhead costs attributable to the manufacturing facilities and process.

Depreciable tangible personal property is assessed for current value by a method known in the property appraisal industry as replacement cost less accrued depreciation. Tables for six (6) ranges of economic life give current value as a percentage of original cost, reflecting both depreciation and appreciation (replacement cost). Floor values reflecting a salvage value of twenty (20) percent of original cost are generally assigned to property that is still in use after the end of its economic life.

Business inventories are generally valued at original cost on a FIFO basis, with book value used as the minimum cash value.

Accounts receivable are reported to the local PVA at their face value, and the PVA deducts an allowance of fifteen (15) percent on the assessed value on accounts less than one (1) year old. Accounts between one (1) and (5) five years old are valued at between eighty-five (85) percent and fifty (50) percent of face value. Accounts over five (5) years are not legally collectable in Kentucky and are given no taxable value.

Property owners that are dissatisfied with the assessment values assigned to their real estate by the local PVA must first request a conference with the PVA. They may then appeal the assessment to the County Board of Assessment Appeals, then to the Kentucky Board of Tax Appeals, and then to the courts.

Exemptions/Rate Reductions

Private leasehold interests in property owned and financed by a governmental unit through industrial revenue bonds, under the provisions of KRS Chapter 103, are taxed by the state at $0.015 per $100 of leasehold value with approval from KEDFA. The same KEDFA approval will exempt the leasehold value from local property taxes. Exemption from local property taxes only on the leasehold value (no state property taxes included), does not require KEDFA approval. Some communities may negotiate for payments by industrial tenants to replace portions of local property taxes lost through public title to the property. Any portions of such projects financed by private capital are subject to the full state and local taxes applicable to private ownership. (KRS 132.020; 132.195; 132.200)

Businesses leasing real estate or personal property from a tax-exempt owner, other than property financed by industrial revenue bonds, must pay full state and local property taxes on their leasehold value. (KRS 132.195)

Cities may exempt the property of new manufacturing facilities from city property taxes for up to five (5) years as an inducement for the location of a plant in the city. This exemption cannot be granted by the state, by counties, by special districts, or by school districts. (KRS 92.300)

Enterprise zones have been established in ten (10) redevelopment areas in Kentucky. Both the city and county may exempt buildings owned by qualifying businesses in an enterprise zone from increases in assessed value for a five (5) year period. In addition, city and county property tax rates may be set as low as 1/10 cent per $100 valuation. (KRS 154.45-090)

Tangible personal property located in a federally designated and activated foreign trade zone (or sub-zone) are exempt from all local property taxes, provided that the zone is activated in accordance with the regulations of the United States Customs Service and the Foreign Trade Zones Board. The state rate is only 1/10 of 1 cent per $100 of assessed value. (KRS 132.020 and 132.200)

City and county governments may grant a moratorium on increases in the assessed value of property taxes of older commercial structures for up to five (5) years following their rehabilitation, repair, restoration, or stabilization by owners or lessees. Structures must be at least twenty (25) years old to qualify. The project becomes eligible for a second assessment moratorium after a three (3) year waiting period. (KRS 99.600)

State law allows for favorable tax treatment for finished goods inventories. The state rate on finished goods inventory is only five (5) cents per $100 of assessed value. Cities, counties, and urban-county governments may exempt or levy rates on these business inventories that are less than the prevailing rate of taxation on other tangible personal property. (KRS 132.020; 68.246; and 132.028)

Personal property placed in a warehouse or distribution center for subsequent distribution to an out-of-state location within six months is exempt from state, city, county, and school district personal property taxes. Finished goods at the end of the manufacturing process that are placed in a warehouse or distribution area for subsequent shipment out-of-state, may qualify for the in transit goods property tax rate. Fire districts and special-taxing districts may exempt property placed in a warehouse or distribution center for subsequent distribution to an out-of-state location at their option. (KRS 132.097 and 132.099)

The state property tax rate is $0.015 per $100 of value on aircraft not used in the business of transporting persons or property for compensation or hire. Local taxing districts may exempt aircraft. (KRS 132.020; 132.200)

Sequence of Events

The property taxation process in Kentucky normally occurs in the following sequence:

1. Between January 1 and May 15, the business owner reports the value of taxable personal property that the business owned on January 1 to the county Property Valuation Administrator (PVA) or the Kentucky Department of Revenue. (KRS 132.220)

2. The PVA sets the assessed value for real property tax purposes. Local real estate assessment rolls are open for public inspection for thirteen (13) days beginning on the first Monday in May.

3. During the summer, the counties, cities, special districts, and school districts set local tax rates for the year. The Kentucky Department of Revenue according to state law sets state rates.

4. Property tax bills are prepared and mailed to taxpayers by late September. Businesses located in cities receive a separate bill for city property taxes.

5. All taxpayers are allowed a two (2) percent discount for paying their property taxes by November 1. Full payment is due by December 31, and payments made later are subject to penalties.

State and Local Property Tax Rates for Business Property
Expressed in Cents Per $100 Dollars of Assessed Value For 2003

Class of Property	**State**	**Counties**	**Cities (1)**	**Schools**
Real Estate	13.3	22.58471	20.81417	47.77598
Manufacturing Machinery	15.0	None	None	None
Pollution Control Facilities	15.0	None	None	None
Inventories				
• Raw Materials & Goods In Progress	5.0	None	None	None
• Finished Goods	5.0	Optional	Optional	48.60
• In Transit Goods (2)	None	None	None	None
Intangibles				
• Accounts Receivable, Money in Hand, Bonds & Notes	25.0	None	None	None
• Accounts from Businesses Conducted Out-of-State (e.g. Credit Card Accounts)	1.5	None	None	None
Leaseholds in Government Owned, Industrial Revenue Bonds (Industrial Facilities) (3)	1.5	None	None	None
Motor Vehicles	45.0	22.968	15.83566	54.58581
Personal Property Operated in an Activated Foreign Trade Zone	0.1	None	None	None
Recycling Machinery & Equipment	45.0	None	None	None
Aircraft (Recreational & Non-Commercial)	1.5	Optional	Optional	Optional
Other Tangible Personal Property (Furniture, Fixtures, Non-Production Equipment, etc.)	45.0	27.728	19.500	48.60
Annuities (Financials)	0.1	None	None	None
Bank Deposits (Kentucky & Out of State)	0.1	None	None	None
Retirement Plans	0.1	None	None	None
Stock Brokers' Accounts Receivable	10.0	None	None	None

1. Average city rates shown inclusive of zero rates.
2. Fire and special districts may exempt or levy a property tax against in transit goods.
3. KEDFA Approved

Click here for [Kentucky State and Local Property Taxes for 2003]

State Sales and Use Tax (KRS 139.010 et seq.)
A state sales tax of six (6) percent is imposed on retailers for the privilege of making retail sales. A retail sale includes the sale, rental, or lease of tangible personal property and the sale of certain services. Taxable services include sewer services, communication services, overnight transient room accommodations, and admissions. Local sales taxes are not levied in Kentucky.

Kentucky's law has been amended to the required provisions of the Streamlined Sales and Use Tax Agreement. The agreement provides for common definitions for key terms, simplified and uniform rules for sourcing transactions, simplified administration of exemptions, and implementation of uniform audit procedures for the administration of sales and use taxes. The agreement is designed to make it easier for online and direct sales businesses to collect and remit sales and use taxes among participating states. (KRS 139.200 through 139.300)

Major exemptions from the state sales tax, important to business and industry in Kentucky, include:

- Trucks weighing over 44,000 pounds are exempt from the motor vehicle usage tax and sales tax on repair and replacement parts. The sales tax exemption is limited to parts for trucks, including any towed unit, used exclusively in interstate commerce for the conveyance of property or passengers for hire.
- Items purchased for resale.
- Machinery for new and expanded industry.
- Raw materials, industrial supplies, and industrial tools.
- Energy and energy producing fuels, to the extent that they exceed three (3) percent of the cost of production.
- Certified pollution control equipment.
- Industrial machinery sold and delivered out-of-state to manufacturers or processors for use out-of-state.
- Containers, packaging, and wrapping materials.
- Motor fuels for highway use.
- Industrial supplies and tools used to perform a manufacturing process on another entity's property.

To qualify for the exemption for new and expanded industry, machinery must meet four (4) specific requirements: (1) it must be machinery; (2) it must be used directly in the manufacturing process; (3) it must be incorporated for the first time into plant facilities in this state; and (4) it must not replace other machinery unless it: increases consumption of recycled materials not less than 10%, performs a different function, manufactures a different product, or has a greater productive capacity. It should be noted that in all cases where a question arises concerning the exemption of machinery for new and expanded industry, the burden of proof that each qualification has been met is upon the one seeking the exemption. (KRS 139.170 section 1)

Manufacturing is defined as a "process through which material having little or no commercial value for its intended use before processing has appreciable commercial value for its intended use after processing by the machinery." The manufacturing process commences with the movement of raw materials from storage into a continuous, unbroken, integrated process and ends when the product is packaged and ready for sale. (KRS 139.170 section 2)

A manufacturing plant facility is a single location exclusively dedicated to manufacturing or processing production activities, with any retail sales only incidental to the manufacturing activities at the location. (KRS 139.170 section 3)

A use tax of six (6) percent is levied on tangible personal property purchased outside of the state for use in Kentucky. The use tax must also be paid on tangible personal property that is purchased for resale but is used instead of sold. The same exemptions allowed to industry for the sales tax are allowed for the use tax. Credit is given for state sales taxes paid out-of-state, if the other state grants similar credits for taxes paid in Kentucky. (KRS 139.310 thru 139.460)

Service businesses such as banks, cleaners, tire repairers, professional services, etc., are classified as consumers of the tangible personal property which they use in rendering their services. (103 KAR 26:010)

Construction contractors are considered the final consumers of building materials, fixtures, and supplies incorporated into buildings and other improvements to real estate (roads, sewers, fences, etc.) and must pay sales and use taxes on such purchases. Contractors are subject to sales and use tax on materials used in contracts with governmental agencies, including facilities financed by government owned industrial revenue bonds. A use tax of six (6) percent is levied on construction machinery, tools, and equipment brought into Kentucky for construction projects. The tax is levied on the original purchase price of the machinery in the same proportion as the duration of its use in Kentucky is to its total useful life. (KRS 139.320)

The sale of business assets held or used in a non-selling activity is exempt from the sales and use tax, unless the sale is one of a series of sales sufficient in number, scope, and character to require the holding of a seller's permit. All sales of assets used in a retail selling activity are subject to the sales tax. (KRS 139.070)

Sales taxes collected by businesses are filed and paid to the Kentucky Department of Revenue once monthly. Some small businesses with limited sales tax collections may be allowed to file less frequently. (KRS 139.540 thru 139.590)

Certified tourism attractions may recover twenty-five (25) percent of the initial project fixed asset costs through a refund of sales tax collected from their admissions and sales of tangible personal property. The recovery period is ten (10) years and is limited to 2.5 percent per annum. The Kentucky Economic Development Finance Authority certifies all tourism attractions and refunds. (KRS 139 and 154)

Sales Tax—Communications Services (Defined)
"Communication services" means the provision, transmission, conveyance, or routing, for a consideration, of voice, data, video, or any other information or signals of the purchaser's choosing to a point, or between or among points, specified by the purchaser, by or through any electronic, radio, light, fiber optics, or any similar medium or method now in existence or later devised. The six (6) percent sales tax shall apply to interstate and intrastate communications services. (KRS 139.100)

(Refundable Credit) State Sales Tax on Communications Services
Any business whose communications service, subject to Kentucky sales tax and deducted for federal income tax purposes, exceeds five percent (5%) of the business's Kentucky gross receipts during the preceeding calendar year is entitled to a refundable credit. The refundable credit shall be equal to the sales tax paid on the difference by which the communications service purchased by the business exceeds five percent (5%) of the business's Kentucky gross receipts. (KRS 139.505)

Kentucky Gross Receipts Defined for Communication Services
Gross receipts for the purpose of determining the refundable tax credit shall be based on that portion of a company's receipts derived from sales occurring in Kentucky. Kentucky gross receipts will be equivalent to the "sales factor" as stated in the apportionment formula found in KRS 141.120. (KRS 139.505)

Utility Gross Receipts License Tax (KRS 160.613 et seq.)
Kentucky statutes allow the imposition of a utility gross receipts license tax for schools not to exceed three (3) percent of the gross receipts derived from the furnishing of intrastate telephonic and telegraphic communications services; electric power; water; natural, artificial, and mixed gas; and the furnishing of cable television services.

"Gross receipts" includes all amounts received in money, credits, property, or other money's worth in any form, as consideration for the furnishing of the above utilities, except that "gross receipts" shall not include amounts received for furnishing energy or energy-producing fuels used in the course of manufacturing, processing, mining, or refining to the extent that the cost of the energy or energy-producing fuels used exceeds three (3) percent of the cost of production, and shall not include amounts received for furnishing any of the above utilities which are to be resold. The consumer shall be held liable for the tax if the seller is exempt by state or federal law. Local schools adopt the Kentucky Revenue Cabinet's ruling for energy exemptions under the sales and use tax. Any utility required to pay the tax may increase its rates by three (3) in any county in which it is required to pay the school tax. Over one hundred (100) of Kentucky's counties currently impose the tax. (KRS 160.613 et seq.)

State Unemployment Insurance (U.I.) Tax (KRS 341)

Most employees in Kentucky are covered by unemployment insurance. Exceptions include commissioned insurance agents, railway workers, some agricultural workers, domestic service employment of less than $1,000 per quarter, student workers, self-employed persons, and employees of certain nonprofit organizations. Covered employees include corporate officers but not owners and partners in unincorporated businesses.

The taxable wage base for U.I. taxes in Kentucky is the first $8,000 of each worker's annual wages, including tips. An individual working forty (40) hours per week at the federal and state minimum wage exceeds the taxable wage within a calendar year.

U.I. tax rates for Kentucky's employers are set annually from statutory tables of rates. The balance in the state U.I. trust fund determines the rate table in effect during a calendar year. An individual employer's contribution rate within the table is determined by its reserve account balance ratio.

Reserve Account Balance Ratio Rate Equals (=)

Reserve Account Balance	Divided (÷) By	Taxable Wages for the Three (3) Previous Years (12 Calendar Quarters)

The statutory table in effect in 2004 has a minimum contribution rate of 0.4 percent of taxable wages for employers with the best reserve account balance ratio, and a maximum rate of nine and one-quarter (9.25%) percent for employers with the poorest reserve ratios. The average employer tax rate was 2.2% in 2002.

A new employer, except contract construction, pays at a rate of at least 2.7 percent of taxable wages during the first three (3) years of operation to establish a reserve account with the state U.I. system; the rate will increase if benefits charged to the account during this time exceed contributions paid. Thereafter it is experience rated, with a contribution rate based on its reserve ratio.

New employers in contract construction pay at the maximum rate under the rate schedule in effect for any given calendar year during the first three (3) years of operation to establish a reserve account with the state U.I. system. Thereafter it is experience rated, with a contribution rate based on its reserve ratio.

Businesses become liable for paying state unemployment insurance taxes by paying at least $1,500 in wages in a calendar quarter, or by employing at least one (1) worker in each of twenty (20) weeks during a calendar year, or by acquiring an existing liable business. Different rules apply for agricultural, domestic and nonprofit employment.

Benefit payments are made from the state U.I. fund to qualified unemployed workers and are charged against the account of the last firm the claimant worked for in each of ten (10) weeks, whether or not consecutive, preceding his/her layoff.

Important Features

- An employer challenging a claim against its account must submit the protest within ten (10) days after notice of the claim is mailed by the Department for Employment Services, Education Cabinet.

- An employer can make voluntary contributions to the state U.I. trust fund to improve its reserve account balance and lower its contribution rate.

- When an operating business is bought by another firm without a significant break in operations, the new owner (successor) assumes the contribution rate and U.I. liabilities of the previous owner.

- When an employer closes down completely, and a new owner reopens the facility, the new company usually starts as new employer, with a contribution rate of 2.7 percent. If the new owner already has a Kentucky account for another location in the state, it assumes the rate of its existing account.

- When an existing employer opens a new business facility, the experienced employer rate is used for the new facility, as long as the new facility is part of the same legal entity. If the new facility is developed as part of a separate legal entity, then the new employer contribution rate of 2.7 percent applies to the new facility.

Appeals Procedures

1. The claimant or employer may appeal the determination on a claim to the Department for Employment Services--Workforce Development Cabinet within fifteen (15) days after the determination is mailed. The Department then appoints a state referee to hear the appeal.

2. An employer or claimant may appeal the referee's decision to the state U.I. Commission within fifteen (15) days after notice of the determination is mailed.

3. The Commission may on its own affirm, modify, or set aside the decision of the referee.

4. Employers or claimants may appeal the Commission’s decision to the circuit court, in the county where the claimant was last employed, within twenty (20) days after the Commission’s decision.

Major Business Taxes in Kentucky

Useful Tax Links

Internal Revenue Service

Kentucky Department of Revenue

Unemployment Insurance

The information provided herein by the Division of Research—Kentucky Cabinet for Economic Development is believed to be accurate but is not warranted and is for informational purposes only. Any estimates, projections, or information provided to make estimates or projections are provided without assurances or warranties and should not be relied upon as fact. Users of the information should perform their own due diligence in drawing conclusions from the information provided.

July 2004